

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

ELECTRONIC APPLICATION OF WESTERN)	
FLEMING COUNTY WATER DISTRICT FOR A)	CASE NO.
RATE ADJUSTMENT PURSUANT TO 807 KAR)	2021-00406
5:076)	

NOTICE OF FILING OF COMMISSION STAFF'S REPORT

Notice is hereby given that, in accordance with the Commission's Order of March 29, 2022, the attached report containing the findings of Commission Staff regarding the Applicant's proposed rate adjustment has been filed in the record of the above-styled proceeding. Pursuant to the Commission's March 29, 2022 Order, Western Fleming County Water District (Western Fleming District) is required to file written comments regarding the findings of Commission Staff no later than 14 days from the date of this report. The Commission directs Western Fleming District to the Commission's July 22, 2021 Order in Case No. 2020-00085¹ regarding filings with the Commission.


Linda C. Bridwell, PE
Executive Director
Public Service Commission
P.O. Box 615
Frankfort, KY 40602

DATED APR 29 2022

cc: Parties of Record

¹ Case No. 2020-00085, *Electronic Emergency Docket Related to the Novel Coronavirus COVID-19* (Ky. PSC July 22, 2021), Order (in which the Commission ordered that for case filings made on and after March 16, 2020, filers are NOT required to file the original physical copies of the filings required by 807 KAR 5:001, Section 8).

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COMMISSION STAFF'S REPORT ON
WESTERN FLEMING COUNTY WATER DISTRICT

Western Fleming County Water District (Western Fleming District), a water district organized pursuant to KRS Chapter 74, provides water service to approximately 1,502 residential and commercial customers in Fleming, Mason, Nicholas, and Robertson counties, Kentucky.¹ In the final Order for Case No. 2019-00456,² Western Fleming District was ordered to file an application by March 30, 2021, for either a traditional adjustment in rates or for an alternative rate adjustment to ensure its revenue is sufficient to support adequate and reliable service. On November 5, 2021,³ Western Fleming District filed its application with the Commission requesting to adjust its water rates pursuant to 807 KAR 5:076.

¹ *Annual Report of Western Fleming County Water District to the Public Service Commission for the Calendar Year Ended December 31, 2020* (2020 Annual Report) at 12 and 49.

² See Case No. 2019-00456, *Electronic Application of Western Fleming County Water District for a Certificate of Public Convenience and Necessity to Construct a System Improvements Project and an Order Approving a Change in Rates and Authorizing the Issuance of Securities Pursuant to KRS 278.023* (Ky. PSC Mar. 30, 2020).

³ Western Fleming District tendered its application on October 28, 2021. By letter dated October 29, 2021, the Commission rejected the application for filing deficiencies. The deficiencies were subsequently cured and the application is deemed filed on November 5, 2021.

To ensure the orderly review of the application, the Commission established a procedural schedule by Order dated December 3, 2021. On December 20, 2021, Western Fleming District filed a letter signed by its Chairman, Vernon Barton, requesting an extension of time to file its responses to Commission Staff's First Request for Information. By its Order dated January 5, 2022, the Commission granted Western Fleming District's request and amended the procedural schedule to extend the remaining deadlines.

On January 19, 2022, Western Fleming District filed a letter seeking Commission approval to withdraw its Alternative Rate Filing (ARF) application. By its Order dated February 9, 2022, the Commission denied Western Fleming District's request to withdraw its ARF application, required Commission Staff to conduct a limited field review, and amended the dates in the procedural schedule. In its March 29, 2022 Order the Commission, upon its own motion, extended the issuance date of the Commission Staff's Report to April 29, 2022.

WATER LOSS

Pursuant to 807 KAR 5:066, Section (6)3, water loss is limited to 15 percent for ratemaking purposes. The Commission Staff notes that Western Fleming District reported a water loss of 23.62 percent in its 2020 Annual Report.⁴ At a 23.62 percent

⁴ 2020 Annual Report at 57.

water loss, the annual cost of water loss in excess of 15 percent is \$26,276 and the total annual cost of water loss to Western Fleming District is \$72,001.⁵

To comply with the requirements of 807 KAR 5:076, Section 9, Western Fleming District based its requested rates on a historic test period that coincides with the reporting period shown in its most recent Annual Report on file with the Commission, the calendar year ended December 31, 2020.⁶

Using the Debt Service Coverage (DSC) method and its pro forma test-year operations in its application, Western Fleming District determined that it could justify a revenue increase of \$10,822, or 0.80 percent.⁷ Western Fleming District is requesting a water loss recovery surcharge of \$1.46 per month per customer to be collected for 48 months.⁸ The rates requested by Western Fleming District, including the water loss recovery surcharge, would increase the monthly bill of a typical residential customer using 4,000 gallons per month by \$1.85, from \$49.47 to \$51.32, or approximately 3.74 percent.⁹

	Purchased Water	Purchased Power	Chemicals	Total
Allowable Purchases	\$ 94,002	\$ 88,784	\$ 122,045	\$ 304,831
Multiplied by: Water Rate per 1,000 Gallons	-8.62%	-8.62%	-8.62%	-8.62%
Cost of Line loss in Excess of the 15% Limit	<u>\$ (8,103)</u>	<u>\$ (7,653)</u>	<u>\$ (10,520)</u>	<u>\$ (26,276)</u>

	Electricity	Purchased Power	Chemicals	Total
Allowable Purchases	\$ 94,002	\$ 88,784	\$ 122,045	\$ 304,831
Multiplied by: Water Rate per 1,000 Gallons	-23.62%	-23.62%	-23.62%	-23.62%
Total Cost of Line Loss	<u>\$ (22,203)</u>	<u>\$ (20,971)</u>	<u>\$ (28,827)</u>	<u>\$ (72,001)</u>

⁶ Application at 3.

⁷ Application, Attachment 4, Revenue Requirements.

⁸ Application, Attachment 1, Customer Notice.

⁹ Application, Attachment 1, Customer Notice. \$49.86 (Monthly Residential Bill Requested Rates) + \$1.46 (Water Loss Reduction Surcharge) = \$51.32 (Total Requested Residential Bill with Surcharge) - \$49.47 (Monthly Residential Bill Existing Rates) = \$1.85 (Total Increase in Residential Monthly Bill) ÷ \$49.47 (Monthly Residential Bill Existing Rates) = 3.74%.

Pro Forma Operating Expenses	\$ 1,110,217
Plus: Average Annual Debt Service	212,592
Debt Service Coverage Requirement	<u>42,518</u>
Overall Revenue Requirement	1,365,328
Less: Other Operating Revenue	(3,657)
Interest Income	<u>(4,565)</u>
Revenue Required from Water Sales	1,357,106
Less: Normalized Revenues from Water Sales	<u>(1,346,284)</u>
Required Revenue Increase/(Decrease)	<u>\$ 10,822</u>
Percentage Increase	<u>0.80%</u>

To determine the reasonableness of the rates requested by Western Fleming District, Commission Staff performed a limited financial review of Western Fleming District's test-year operations. The scope of Commission Staff's review was limited to determining whether operations reported for the test year were representative of normal operations. Known and measurable changes to test-year operations were identified and adjustments were made when their effects were deemed material. Insignificant and immaterial discrepancies were not necessarily pursued or addressed.

Commission Staff's recommendations are summarized in this report. Mark Frost reviewed Western Fleming District's Pro Forma Operating Expenses and its Overall Revenue Requirement. Eddie Beavers reviewed Western Fleming District's reported revenues and rate design.

SUMMARY OF FINDINGS

1. Overall Revenue Requirement and Required Revenue Increase. By applying the DSC method, as generally accepted by the Commission, Commission Staff found that Western Fleming District's required Overall Revenue Requirement is \$1,386,521. To meet the Overall Revenue Requirement, Western Fleming District

requires a \$32,015 or 2.38 percent revenue increase to Pro Forma present rate revenues. If Western Fleming District wishes to request that the Commission approve a revenue increase of the amount calculated by Commission Staff, it should do so in its written response to this report.

2. Monthly Water Service Rates. Western Fleming District proposed to increase all of its monthly retail and wholesale water service rates by approximately 0.80 percent across the board. Western Fleming District did not file a cost of service study (COSS). Western Fleming District also did not state why a COSS was not filed.¹⁰

The Commission has previously found that the allocation of a revenue increase evenly across the board to a utility's rate design is appropriate when there has been no evidence entered into the record demonstrating that this method is unreasonable and in the absence of a COSS. Finding no such evidence in this case, Commission Staff has followed the method previously accepted by the Commission and has allocated the \$32,015 revenue increase evenly across the board to Western Fleming District's monthly retail and wholesale water service rates.

Western Fleming District currently has several customers that are connected on a single meter. Multiple customers on a single meter are either those that are grandfathered in prior to February 22, 2022, have a special contract, or were otherwise approved by Western Fleming District.¹¹

¹⁰ Western Fleming District's Responses to Commission Staff's First Request for Information (Staff's First Request) (filed Dec. 20, 2022), Items 3 and 4.

¹¹ See, Western Fleming District Tariff PSC Ky. No 1 Original Sheet No. 14, Rules and Regulations, Section C(f).

The rates set forth in Appendix A to this report are based upon the revenue requirement, as calculated by Commission Staff, and will produce sufficient revenues from water sales to recover the \$1,378,299 Revenue Required from Rates, an approximate 2.38 percent increase. These rates will increase a typical residential customer's monthly water bill from \$49.47 to \$52.12, an increase of \$2.65, or approximately 5.36 percent.¹²

3. Nonrecurring Charges. Following the Commission's recent decisions,¹³ Commission Staff has reviewed Western Fleming District's nonrecurring charges. The Commission found that as district personnel are currently paid during normal business hours, estimated labor costs previously included in determining the amount of Nonrecurring Charges should be eliminated from the charges. Commission Staff has reviewed the most recent cost justification information provided in the response to Commission Staff's First Request.¹⁴ Such adjustments result in the following revised nonrecurring charges:

Nonrecurring Charges	
Connection/Turn On Charge	\$20.00
Reconnection Charge	\$30.00
Reconnection Charge, After Hours	\$75.00
Return Check Charge	\$3.00

¹² The typical residential customer uses approximately 4,000 gallons per month. This calculation includes the \$1.46 surcharge.

¹³ Case No. 2020-00141, *Electronic Application of Hyden-Leslie County Water District for an Alternative Rate Adjustment* (Ky. PSC Nov. 6, 2020) and Case No. 2020-00167, *Electronic Application of Ohio County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 3, 2020), Case No. 2020-00196, *Electronic Application of West Daviess County Water District for an Alternative Rate Adjustment* (Ky. PSC Dec. 30, 2020), and Case No. 2020-00195 *Electronic Application of Southeast Daviess County Water District for an Alternative Rate Adjustment*, (Ky. PSC Dec. 30, 2020).

¹⁴ Western Fleming District's Response to Staff's First Request (provided at field review held Mar. 22, 2022), Item 16.

Service Call Charge	\$20.00
Service Call Charge, After Hours	\$50.00
Service Line Inspection	\$30.00

The adjustments to the Nonrecurring Charges would normally result in a decrease to the charges and an increase to the total revenue requirement. Western Fleming District was unable to provide appropriate information concerning the nonrecurring charges and occurrences actually occurring throughout the test year to properly adjust the revenues of the nonrecurring charges.¹⁵ Therefore Commission Staff is unable to make an adjustment to the total revenue requirement based upon the reduction in charges listed in the table above.

PRO FORMA OPERATING STATEMENT

Western Fleming District's Pro Forma Operating Statement for the test year ended December 31, 2020, as determined by Commission Staff, appears below.

¹⁵ At the Field Review on March 22, 2022, the Office Manager could not verify or explain the information compiled and was unable to explain the differences in this information and the reported information included in the 2020 Annual Report for the test year concerning the nonrecurring charges.

	Test Year Operations	Pro Forma Adjustments	Adj. Ref.	Pro Forma Operations
Operating Revenues:				
Total Metered Sales	\$ 1,282,838	\$ (385,213)	A	
		11,173	A	
		23,790	B	\$ 932,588
Sales for Resale		385,213	A	
		28,483	B	413,696
Total Revenue - Water Sales	1,282,838	63,446		1,346,284
Other Water Revenues:				
Misc. Service Revenues	21,630	(11,173)	A	
		(6,800)	A	3,657
Total Operating Revenues	1,304,468	45,473		1,349,941
Operating Expenses:				
Operation and Maintenance:				
Salaries and Wages - Employees	252,332	27,073	C	
		(2,040)	D	277,365
Salaries and Wages - Officers	22,800	1,200	E	24,000
Employee Pensions and Benefits	88,347	15,602	F	
		(10,434)	G	93,515
Purchased Water	94,002	(8,104)	H	85,898
Purchased Power	88,784	(7,654)	H	81,130
Chemicals	122,045	(10,522)	H	111,523
Materials and Supplies	44,355	(4,760)	D	39,595
Contractual Services	91,825			91,825
Insurance - Gen. Liab. & Workers Comp.	20,993			20,993
Bad Debt	30,188	(88)	I	30,100
Miscellaneous Expenses	32,305			32,305
Total Operation and Maint. Expenses	887,976	273		888,249
Depreciation Expense	244,018	(22,235)	J	221,783
Taxes Other Than Income	21,375	(1)	K	21,374
Total Operating Expenses	1,153,369	(22,236)		1,131,406
Net Utility Operating Income	\$ 151,099	\$ 67,709		\$ 218,535

(A) Revenue Reclassification. In preparing its application, Western Fleming District discovered that it had incorrectly recorded Sales for Resale of \$385,213, Sales to

Public Authorities of \$11,173 and tap-on fees of \$6,800.¹⁶ Western Fleming District proposed the following adjustments to correct the misclassified revenues.¹⁷

Account Title	Debit	Credit
Total Metered Sales	\$ 11,173	
Sales for Resale	\$ 385,213	
Misc. Service Revenues	\$ 6,800	
Misc. Service Revenues		\$ 11,173
Total Metered Sales		\$ 385,213

In reviewing the 2020 General Ledger, Commission Staff determined that Western Fleming District did incorrectly record Sales for Resale, Sales to Public Authorities, and tap-on fees in the wrong accounts. Accordingly, Commission Staff is accepting Western Fleming District's proposed correcting adjustments.

(B) Billing Analysis. Western Fleming District proposed to adjust its test-year retail revenues from water sales of \$1,282,838 by the following: (1) a decrease of \$385,213 to reflect the Sales for Resales that were misclassified during the test year; (2) an increase of \$11,173 for Sales for Public Authority that were misclassified as Other Water Revenues during the test year; and (3) an increase of \$23,790 to general Total Metered Water Sales and \$28,483 to Sales for Resales account for the rate increase that was implemented in in Case No. 2019-00456.¹⁸ Western Fleming District's adjustment

¹⁶ Application, Attachment 4, Schedule of Adjusted Operations, Ref. A and Ref. B, References, Ref. A and Ref B.

¹⁷ Application, Attachment 4, Schedule of Adjusted Operations, Ref. A and Ref. B, References, Ref. A and Ref B.

¹⁸ Case No. 2019-00456, *Electronic Application of Western Fleming County Water District for a Certificate of Public Convenience and Necessity to Construct a System Improvements Project and an Order Approving a Change in Rates and Authorizing the Issuance of Securities Pursuant to KRS 278.023* (Ky. PSC Mar. 20, 2020).

meets the ratemaking criteria of being known and measurable and Commission Staff accepts the adjustment in Pro Forma operations.

(C) Salaries and Wages - Employees. Western Fleming District proposed to increase its test year Employee Salaries and Wages expense of \$252,332 by \$23,371 for a pro forma Employee Salaries and Wages expense of \$275,703.¹⁹ The proposed adjustment reflects the wage increases Western Fleming District has given its employees since 2020.²⁰

An adjustment to reflect Western Fleming District's 2022 wage rates would meet the ratemaking criteria of being known and measurable.²¹ Using Western Fleming District's current staff level of six full-time employees, two part-time employees, the hours that each employee worked in the test year,²² and the 2022 employee wage rates, Commission Staff calculates a pro forma employee Salaries and Wages expense of \$279,405, which is \$27,073, above the reported level of \$252,332, as calculated in the table below.

¹⁹ Application, Attachment 4, Schedule of Adjusted Operations, Ref. D, and References, Ref. D.

²⁰ Application, Attachment 4, References, Ref. D.

²¹ See, 807 KAR 5:001, Section 16.1.(a).; Case No. 2001-00211, *The Application of Hardin County Water District No. 1 for (1) Issuance of Certificate of Public Convenience and Necessity; (2) Authorization to Borrow Funds and to Issue Its Evidence of Indebtedness Therefor; (3) Authority to Adjust Rates; and (4) Approval to Revise and Adjust Tariff* (Ky. PSC Mar. 1, 2002); Case No. 2002-00105, *Application of Northern Kentucky Water District for (A) an Adjustment of Rates; (B) a Certificate of Public Convenience and Necessity for Improvements to Water Facilities if Necessary; and (C) Issuance of Bonds* (Ky. PSC June 25, 2003); Case No. 2017-00417, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of Lebanon Water Works* (Ky. PSC July 12, 2018); and Case No. 2019-00080, *Electronic Proposed Adjustment of the Wholesale Water Service Rates of the City of Pikeville to Mountain Water District* (Ky. PSC Dec. 19, 2019).

²² Employee regular hours worked in the test-year is limited to 2,080 hours. Any new employees hired after 2020 are assumed to work 2,080 annual regular hours.

Employee Name	Job Description	Status	Hire Date	2020 Hours Worked		2021 Wage Rates	Emp. Salaries And Wages
				Regular	Overtime		
Hinton, Richard	Water Plant	Full-Time	08/13/18	2,238.00	71.25	20.00	\$ 46,898
Knight, James	Water Plant	Part-Time		290.50	0.00	19.30	5,607
Mitchell, Melvin D	Water Plant	Full-Time	08/20/07	2,080.00	0.00	29.13	60,590
Grayson, Faron	Water Plant	Full-Time	06/21/21	2,080.00	0.00	17.00	35,360
Engle, Travis	Water Plant	Full-Time	11/22/21	2,080.00	0.00	17.50	36,400
Hazelrigg, Alison	Office Manager	Full-Time	11/29/21	2,080.00	0.00	16.00	33,280
Shrout, Arlene	Office Clerk	Part-Time	09/01/18	382.25	0.00	13.93	5,325
Syck, Jason	Outside Labor	Full-Time	06/23/14	2,189.75	127.25	23.50	55,945
Pro Forma Employee Salaries & Wages							279,405
Less: Pro Forma Employee Salaries & Wages - Staff Report							(252,332)
Pro Forma Adjustment							\$ 27,073
Gross Wages for Full Time Employees CERS Eligible							\$ 268,473

(D) Tap-on Fees. During the test year, Western Fleming District collected tap-on fees of \$6,800.²³ Western Fleming District explained that its new meter installations were installed by District employees and that the cost of the installations (labor and material) were incorrectly recorded as operating expenses.²⁴ Substituting the tap-on fees for the actual costs it incurred to install the meters, Western Fleming District proposed to deduct 30 percent of the collected tap-on fees or \$2,040 from Salaries and Wages expense and the remaining 70 percent or \$4,760 from the Materials and Supplies expense.²⁵ Commission Staff finds that Western Fleming District's adjustments meet the ratemaking criteria of being known and measurable, and Commission Staff accepts Western Fleming District's adjustments.

(E) Salaries and Wages - Commissioners. Western Fleming District proposed to increase its test year Commissioner Salaries and Wages expense of \$22,800 by \$1,200 for a pro forma Commissioner Salaries and Wages expense of \$24,000.²⁶ According to Western Fleming District a previously vacant Commissioner position has

²³ Application, Attachment 4, Schedule of Adjusted Operations, Ref. J, and References, Ref. J.

²⁴ Application, Attachment 4, References, Ref. J.

²⁵ Application, Attachment 4, References, Ref. J.

²⁶ Application, Attachment 4, Schedule of Adjusted Operations, Ref. G, and References, Ref. G.

been filled, which resulted in is proposed increase of \$1,200. In 2022 there are five active members on Western Fleming District Board of Commissioners and each member is paid \$400 per month or \$4,800 annually. This results in a pro forma Commissioner Salaries and Wages expense of \$24,000, the level proposed by Western Fleming District.

(F) County Employee Retirement System (CERS). Western Fleming District reported a test-year CERS expense of \$56,751.²⁷ Western Fleming District proposed to decrease its test year CERS expense of \$56,751 by \$1,608 for a pro forma CERS expense of \$55,143.²⁸ According to Western Fleming District the increase in employee wages coupled with the increased employer's CERS contribution rate was more than offset by fewer employees participating.²⁹ The combination of these factors resulted in Western Fleming District's estimated CERS expense decrease of \$1,608.³⁰

Western Fleming District provides pension benefits and post-retirement health care benefits to its employees by participating in the CERS. As a participating member, Western Fleming District is required to contribute a percentage of its employee wages to CERS. The CERS pension expense Western Fleming District reported in the test year conformed to the requirements of the General Accounting Standards Board Pronouncement No. 68 (GASB 68).

²⁷ Western Fleming District's Responses to Staff's First Request (filed Dec. 20, 2021), Item 11, Excel Workbook: 11_Rate_Study.xlsx; Tab: Wages.

²⁸ Application, Attachment 4, Schedule of Adjusted Operations, Ref. E, and References, Ref. E.

²⁹ Application, Attachment 4, References, Ref. E.

³⁰ Application, Attachment 4, References, Ref. E.

In Case No. 2016-00163,³¹ the Commission discussed in great detail the reporting requirements of GASB 68, and how those requirements would impact a utility's income statement and balance sheet. In that proceeding, the Commission found the annual pension expense should be equal to the amount of a district's contributions to CERS, which historically have been "fairly constant." In the fiscal year, beginning July 1, 2021, the CERS employer contribution rate increased to 26.95 percent.³² Based on the above, Commission Staff determined that Western Fleming District's pro forma CERS employer contributions are \$72,353,³³ resulting in an increase to Employee Pensions and Benefits expense of \$15,602.³⁴

(G) Employee Benefits. Western Fleming District reported paying test-year employee insurance premiums (Employee Benefits) of \$31,956.³⁵ Western Fleming District proposed to decrease its test year Employee Benefits expense of \$31,926 by \$10,428 for a pro forma expense level of \$21,528.³⁶ Western Fleming District currently pays 100 percent of the monthly premiums for single health coverage, vision, dental, and life insurance for its eligible full-time employees.³⁷ Western Fleming District explained that the Commission requires the expenses associated with this level of employer-funded

³¹ Case No. 2016-00163, *Alternative Rate Adjustment filing of Marion County Water District* (Ky. PSC Nov. 10, 2016).

³² <https://kyret.ky.gov/Employers/Pages/Contribution-Rates.aspx>

³³ \$268,473 (Gross Wages for Full Time Employees CERS Eligible) x 26.95% (July 1, 2020 CERS Employer Contribution Rate) = \$72,353.

³⁴ \$72,353 (Pro Forma CERS Contribution) - \$56,751 (Test-Year CERS Contribution) = \$15,602.

³⁵ Western Fleming District's Responses to Staff's First Request, Item 11, Excel Workbook: 11_Rate_Study.xlsx; Tab: Medical.

³⁶ Application, Attachment 4, Schedule of Adjusted Operations, Ref. K, and References, Ref. K.

³⁷ Application, Attachment 4, References, Ref. K.

employee insurance premiums be adjusted to be consistent with the Bureau of Labor Statistics' national average for an employer's share of health insurance premiums.³⁸ Wester Fleming District stated that the Commission currently places the following employer contribution limitations on employee insurance benefits: a 79 percent limit single employee health insurance coverage, a 66 percent on family coverage, and a 60 percent limitation dental coverage.³⁹ Applying those percentages to the current employee insurance premiums is the basis of Western Fleming District's proposed adjustment.⁴⁰

Commission Staff notes that the Commission has consistently made ratemaking adjustments to reduce the cost of employee benefit packages paid by some utilities when certain aspects of those benefit packages were found to be unreasonable based on a review of total salaries and fringe benefits. The Commission continues to place greater emphasis on evaluating employees' total compensation packages, including both salary and benefits programs, for market and geographic competitiveness to ensure the development of a fair, just, and reasonable rate. It has found that, in most cases, 100 percent of employer-funded health care does not meet those criteria.

Consistent with past precedent, in which the Commission has reduced benefit expenses for utilities that pay 100 percent of an employee's health insurance coverage; Commission Staff reduced Western Fleming District's single health insurance premiums by 22 percent for individual health insurance, 34 percent for family/parent plus

³⁸ Application, Attachment 4, References, Ref. K.

³⁹ Application, Attachment 4, References, Ref. K.

⁴⁰ Application, Attachment 4, References, Ref. K.

insurance,⁴¹ and by 60 percent dental insurance, the national average employee contribution rate.⁴² Factoring in the preceding, Commission Staff decreased employee pensions and benefits by \$10,434, as shown in the calculation below.

	Monthly Premium	District Contirb %	Annual Premium	Allowable Employer Share	Allowable Employer Premium
Medical	\$ 2,197	100%	\$ 26,364	79%	\$ 20,828
Vision	6	100%	72	100%	72
Dental	33	100%	396	60%	238
Administrative	32	100%	384	100%	384
TOTAL	\$ 2,268		\$ 27,216		\$ 21,522
Allowable Employer Premium					\$ 21,522
Less Annual Premium					(31,956)
Medical Adjustment					<u>\$ (10,434)</u>

(H) Excess Water Loss. Commission regulation 807 KAR 5:066, Section 6(3)⁴³ limits water loss to 15 percent for ratemaking purposes unless the Commission finds an alternative level reasonable. Western Fleming District reported a test-year water loss of 23.62 percent, or 8.62 percentage points above the 15 percent allowable limit.⁴⁴ To

⁴¹ Bureau of Labor Statistics, Healthcare Benefits, March 2020, Table 3, private industry workers. (<https://www.bls.gov/news.release/pdf/ebs2.pdf>).

⁴² The Willis Benchmarking Survey, 2015, at 62–63. (https://www.willis.com/Documents/publications/Services/Employee_Benefits/20151230_2015WillisBenefitsBenchmarkingSurveyReport.pdf).

⁴³ “Unaccounted-for water loss. Except for purchased water rate adjustments for water districts and water associations, and rate adjustments pursuant to KRS 278.023(4), for ratemaking purposes a utility’s unaccounted-for water loss shall not exceed fifteen (15) percent of total water produced and purchased, excluding water used by a utility in its own operations. Upon application by a utility in a rate case filing or by separate filing, or upon motion by the commission, an alternative level of reasonable unaccounted-for water loss may be established by the commission. A utility proposing an alternative level shall have the burden of demonstrating that the alternative level is more reasonable than the level prescribed in this section.”

⁴⁴ 2020 Annual Report at 57.

eliminate the cost to purchase, produce and pump water over the 15 percent allowable limit, Western Fleming District proposed to decrease Purchased Water expense, Purchased Power expense and Chemical expense by \$8,104, \$7,654, and \$10,522, respectively.⁴⁵ Commission Staff finds that Western Fleming District's proposal to eliminate the costs associated with excessive water loss conforms to the Commission's current practice and, therefore, is accepting Western Fleming District's adjustments to Purchased Water expense, Purchased Power expense and Chemical expense.

Western Fleming District requests a Water Loss Reduction Surcharge of \$1.46 per customer per month for 48 months to help lower system losses to more acceptable levels.⁴⁶ As calculated above, adjustments to Purchased Water expense, Purchased Power expense and Chemical expense amount to \$26,276⁴⁷ and this amount should be collected and set aside as a surcharge fund. The use of a surcharge is consistent with prior Commission action in cases involving water districts with excessive unaccounted-for water loss. In establishing water-loss surcharges, the Commission recognized that the adjustments required to be made to comply with the 15 percent line-loss limitation in 807 KAR 5:066, Section 6(3), could severely restrict cash flow and could impair a water district's ability to take the necessary action to focus on its leak detection and repair. Using a surcharge to fund a water district's water loss reduction project allows the Commission to place strict controls governing the surcharge proceeds to ensure their effective use, public acceptance of the surcharge, and public confidence in the water

⁴⁵ Application, Attachment 4, Schedule of Adjusted Operations, Ref. H, and References, Ref. H.

⁴⁶ Application, Attachment 1, Customer Notice.

⁴⁷ \$8,104 (Purchased Water) + \$7,654 (Purchased Power) + \$10,522 (Chemicals) = \$26,280.

district's use of those funds. In its report entitled, "*Confronting the Problems Plaguing Kentucky's Water Utilities: An Investigative Report by the Kentucky Public Service Commission November 2019*" that was fully incorporated in the final Order in Case No. 2019-00041, Appendix L, the Commission recommended more frequent rate cases and pursuing qualified infrastructure improvement surcharges, the proceeds of which will be devoted exclusively to infrastructure improvement and replacement.

Western Fleming District should develop and submit a qualified infrastructure improvement plan in furtherance of the recommendations from Case No. 2019-00041 to be approved by the Commission and use the surcharge funds to further reduce its water loss as part of that plan. A monthly surcharge is a reasonable means for Western Fleming District to recover the cost of an infrastructure improvement and water leak detection program in order to reduce the increased expense and lost revenue from unaccounted-for water loss.

Western Fleming District should assess a monthly water loss reduction surcharge of \$1.46 per active customer over 48 months. Western Fleming District should be permitted to assess a surcharge to fund its unaccounted-for water loss reduction efforts to comply with the Commission's final Order in Case No. 2019-00041. Western Fleming District should be restricted to expending any funds collected under the surcharge subject to authorization by the Commission. Western Fleming District should file a qualified infrastructure improvement plan, including a comprehensive unaccounted-for water loss reduction plan that establishes priorities, a time schedule for eliminating each source of unaccounted-for water loss, and provides a detailed spending plan for the proceeds of the requested surcharge.

(I) Bad Debt. Western Fleming District proposed to decrease its test-year Bad Debt expense of \$30,188 by \$88 for a pro forma Depreciation expense of \$30,100.⁴⁸ In preparing its application, Western Fleming District discovered that Bad Debt expense was overstated in its 2020 Annual Report by \$88.⁴⁹ Commission Staff believes that Western Fleming District's adjustment to correct the reporting error made in the 2020 Annual Report is reasonable and that it meets the rate making criteria of being known and measurable. Commission Staff is decreasing Bad Debt expense by \$88.

(J) Depreciation. Western Fleming District proposed to decrease its test-year Depreciation expense of \$244,018 by \$22,235⁵⁰ for a pro forma Depreciation expense of \$221,783.⁵¹ Western Fleming District explained that it has a water main construction project costing \$1,972,331 that will be completed and placed in service in 2022.⁵² The new water main has been included in Western Fleming District's depreciation schedule.⁵³ According to Western Fleming District, the Commission typically requires a water utility to adjust its depreciation expense when its depreciation lives fall outside of the ranges recommended in the report published in 1979 by the National Association of Regulatory Utility Commissioners (NARUC) titled Depreciation Practices for Small Water Utilities (NARUC Study).⁵⁴ Western Fleming District claims that its proposed adjustment brings

⁴⁸ Application, Attachment 4, Schedule of Adjusted Operations, Ref. I, and References, Ref. I.

⁴⁹ Application, Attachment 4, References, Ref. I.

⁵⁰ (\$22,785) (Revised Depreciation Life Adjustment) + \$551 (Audit Adjustment) = \$22,235.

⁵¹ Application, Attachment 4, Schedule of Adjusted Operations, Ref. L and Ref. M, and References, Ref. L and Ref. M.

⁵² Application, Attachment 4, References, Ref. M.

⁵³ Application, Attachment 4, References, Ref. M.

⁵⁴ Application, Attachment 4, References, Ref. M.

the depreciable lives of its assets to or near the midpoint of NARUC's recommended ranges.⁵⁵ Also, included in Western Fleming District's proposed Depreciation Expense adjustment is an 2020 Audit correction of \$551.⁵⁶

Upon its review of Western Fleming District's depreciation schedule, Commission Staff determined that Western Fleming District's adjusted depreciation lives are at the midpoint of the NARUC Study range for each asset category. Further, the adjustments to include the main under construction and the 2020 Audit adjustment would meet the rate making criteria of being known and measurable. Commission Staff believes Western Fleming District's net depreciation adjustment to be reasonable and has decreased Depreciation expense by \$22,235.

(K) Payroll Taxes. Western Fleming District proposed to decrease its test year Payroll Tax expense of \$21,375 by \$284 to a pro forma level of \$21,091 to reflect its Pro Forma Salaries and Wages changes.⁵⁷

In reviewing Western Fleming District's payroll records, Commission Staff discovered that Western Fleming District paid FICA taxes of \$1,836 for its commissioners. For tax purposes commissioners would not be classified as employees, but rather are

⁵⁵ Application, Attachment 4, References, Ref. M.

⁵⁶ Application, Attachment 4, References, Ref. L.

⁵⁷ Application, Attachment 4, Schedule of Adjusted Operations, Ref. F and References, Ref. F.

treated as independent contractors.⁵⁸ As an independent contractor the commissioners are responsible to pay 100 percent of their Self-Employment Tax (SE tax)⁵⁹ and are not subject to income tax (federal, state, or local) withholdings from their fees. Eliminating the FICA tax paid for the Commissioners would result in a revised test-year Payroll Tax expense of \$19,539.

Using the pro forma Employee Salaries and Wages expense of \$255,237 and the current FICA rate of 7.65 percent, Commission Staff calculated a pro forma FICA expense of \$21,374.⁶⁰ This would result in an increase of \$1,835 to the revised payroll tax expense of \$19,539.⁶¹ The net impact to Western Fleming District's reported Payroll Tax expense of \$21,375 is a decrease of \$1.⁶²

⁵⁸ Exempt Organizations: Who Is a Statutory Non-Employee? Internal Revenue Service (irs.gov). Applicable for tax-exempt organizations under Internal Revenue Code (IRC) 501(c)(3).

Directors of a corporation - members of the governing board - are defined by statute as non-employees. If an exempt organization pays its board members to attend board meetings or otherwise compensates them for performing their duties as directors, the organization should treat them as independent contractors. (The director fee is reported on Form 1099-NEC.) This is the most common type of statutory non-employee that may be involved in an exempt organization.

⁵⁹ SE tax is similar to the FICA taxes. With FICA taxes, half of the taxes are withheld from the employee paycheck and the other half is paid by the employer. But with SE tax, the Commissioner is responsible to pay the entire tax.

⁶⁰ \$279,405 (Pro Forma Employee Salaries and Wages expense) x 7.65% (FICA Rate) = \$21,374.

⁶¹ \$21,374 (Pro Forma Payroll Tax) - \$19,539 (Revised Payroll Tax) = \$1,835.

⁶² \$1,835 (Normalized FICA Adjustment) - \$1,836 (FICA Adjustment for Commissioners) = \$1.

OVERALL REVENUE REQUIREMENT AND
REQUIRED REVENUE INCREASE

The Commission has historically applied a DSC method to calculate the revenue requirement of water districts and water associations.⁶³ This method allows for recovery of (1) cash-related pro forma operating expenses; (2) recovery of depreciation expense, a non-cash item, to provide working capital; (3) the average annual principal and interest payments on all long-term debts, and (4) working capital that is in addition to depreciation expense.

A comparison of Western Fleming District's and Commission Staff's calculations of the revenue requirement and required revenue increase using the DSC method is shown below:

	<u>Western Fleming District</u>	<u>Commission Staff</u>
Pro Forma Operating Expenses	\$ 1,110,217	\$ 1,131,406
Plus: Average Annual Debt Service	212,592	212,592
Debt Service Coverage Requirement	<u>42,518</u>	<u>42,518</u>
Overall Revenue Requirement	1,365,327	1,386,517
Less: Other Operating Revenue	(3,657)	(3,657)
Interest Income	<u>(4,565)</u>	<u>(4,565)</u>
Revenue Required from Water Sales	1,357,105	1,378,295
Less: Normalized Revenues from Water Sales	<u>(1,346,284)</u>	<u>(1,346,284)</u>
Required Revenue Increase/(Decrease)	<u>\$ 10,821</u>	<u>\$ 32,011</u>
Percentage Increase	<u>0.80%</u>	<u>2.38%</u>

⁶³ See Case No. 2019-00424, *Electronic Application of Grant County Sanitary Sewer District for an Alternate Rate Adjustment* (Ky. PSC May 6, 2020); see also Case No. 2019-00268, *Application of Knott County Water and Sewer District for an Alternative Rate Adjustment* (Ky. PSC Jan. 31, 2020).

Average Annual Principal and Interest Payments.

At the time of Commission Staff's review, Western Fleming District had an outstanding loan from the Kentucky Infrastructure Authority (KIA)⁶⁴ and four outstanding bond issuances from the U.S. Department of Agriculture's Rural Development (RD).⁶⁵ In calculating its revenue requirement, Western Fleming District used an average annual debt service of \$212,592 and a 0.2 DSC of \$42,518.⁶⁶ Upon its review of Western Fleming District's debt amortization schedules, Commission Staff verified that Western Fleming District's calculations are correct.

⁶⁴ Case No. 2014-00400, *Western Fleming County Water District and its Individual Commissioners, Vernon Barton, James Huston; Larry Ingram; Billy McIntyre, Anthony Overby, And Fred Rose Alleged Failure to Comply with KRS 278.020(1) and KRS 278.300(1)* (Ky. PSC Mar. 16, 2015). The Commission initiated this Show Cause proceeding for Western Fleming District's failure to obtain a Certificate of Public Convenience and Necessity prior to beginning construction of a major project at Western Fleming District's water treatment facilities and for failing to request an order from the Public Service Commission authorizing Western Fleming District to enter into a KIA loan to finance this project.

⁶⁵ Case No. 10024. *The Application of The Western Fleming Water District of Fleming County, Kentucky for Approval of Construction and Financing* (Ky. PSC May. 12, 1988); Case No. 1997-00387, *In the Matter of the Application of Western Fleming County Water District of Fleming County, Kentucky, for a Certificate of Public Convenience and Necessity to Construct, Finance and Increase Rates Pursuant to KRS 278.023* (Ky. PSC Oct. 8, 1997); Case No. 2002-00290, *Application of Western Fleming County Water District for a Certificate of Public Convenience and Necessity to Construct, Finance and Increase Rates Pursuant to KRS 278.023* (Ky. PSC Aug. 29, 2002); and Case No. 2019-00476, *Electronic Application of Western Fleming County Water District for a Certificate of Public Convenience and Necessity to Construct a System Improvements Project and an Order Approving a Change in Rates and Authorizing the Issuance of Securities Pursuant to KRS 278.023* (Ky. PSC Mar. 30, 2020).

⁶⁶ Western Fleming District's Responses to Staff's First Request, Item 11, Excel Workbook: 11_Rate_Study.xlsx; Tab: Debt Service.

Signatures

/s/Mark Frost_____

Prepared by: Mark Frost
Revenue Requirement Branch
Division of Financial Analysis

/s/ Eddie Beavers_____

Prepared by: Eddie Beavers
Rate Design Branch
Division of Financial Analysis

APPENDIX

APPENDIX TO COMMISSION STAFF'S REPORT OF THE KENTUCKY PUBLIC SERVICE COMMISSION IN CASE NO. 2021-00406 DATED APR 29 2022

The following rates and charges are prescribed for the customers in the area served by Western Fleming County Water District. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under the authority of the Commission prior to the effective date of this Order.

Monthly Water Rates

5/8- x 3/4-Inch Meter

First	1,000 Gallons	\$ 19.07	Minimum Bill
Next	6,000 Gallons	0.01053	Per Gallon
Next	3,000 Gallons	0.00866	Per Gallon
Over	10,000 Gallons	0.00693	Per Gallon

Multiple Connections

1 Connection	1,000 Gallons	\$ 19.07	Minimum Bill
2 Connections	2,000 Gallons	38.14	Minimum Bill
3 Connections	3,000 Gallons	57.21	Minimum Bill
5 Connections	5,000 Gallons	95.35	Minimum Bill
6 Connections	6,000 Gallons	114.42	Minimum Bill

Water Loss Reduction Surcharge \$1.46 Per Customer

Wholesale Rates \$ 0.00219 Per Gallon

Nonrecurring Charges

Connection/Turn On Charge	\$20.00
Reconnection Charge	\$30.00
Reconnection Charge, After Hours	\$75.00
Return Check Charge	\$3.00
Service Call Charge	\$20.00
Service Call Charge, After Hours	\$50.00
Service Line Inspection	\$30.00

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